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No. 90-987

In the Supreme Court of the United States

OCTOBER TERM, 1990

CHURCH OF SCIENTOLOGY OF CALIFORNIA, PETITIONER

v.

UNITED STATES OF AMERICA, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

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QUESTION PRESENTED

Whether, in accordance with this Court's judgment in *United States* v. *Zolin*, 109 S. Ct. 2619, 2632 (1989), remanding this case for further proceedings consistent with its opinion, the court of appeals correctly held that the tapes of two meetings of the Mission Corporate Category Sortout (MCCS) project were within the scope of the crime-fraud exception to the attorney-client privilege.

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OPINION BELOW

The opinion of the court of appeals (Pet. App. 2a-4a), following remand from this Court in *United States* v. *Zolin*, 109 S. Ct. 2619 (1989), is reported at 905 F.2d 1344.

JURISDICTION

The judgment of the court of appeals was entered on June 20, 1990, and a petition for rehearing was denied on September 19, 1990. Pet. App. 1a. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. This case arises out of the efforts of the Criminal Investigation Division of the Internal Revenue Service (IRS) to investigate the tax returns of L. Ron Hubbard, the

founder of the Church of Scientology of California, and others for tax years 1979-1983. In the course of the investigation, the IRS sought access to 49 documents that had been filed with the Clerk of the Los Angeles County Superior Court in connection with a case entitled *Church of Scientology* v. *Armstrong*, No. C420 153 (Feb. 11, 1985). In October 1984, the IRS served an administrative summons on the Clerk of the Superior Court seeking a number of documents contained in the record of the *Armstrong* case relating to the Church's activities. The Clerk's office produced some of the documents, but it refused to produce 13 documents that had been ordered sealed by the Superior Court. The government then instituted this proceeding in the United States District Court for the Central District of California to enforce the summons. Pet. App. 18a. See *United States* v. *Zolin*, 109 S. Ct. 2619, 2623-2624 (1989).

Petitioner and Mary Sue Hubbard intervened to oppose production of the sealed documents. They contended, inter alia, that the IRS was not seeking the summoned documents in good faith and objected on grounds of lack of relevance and attorney-client privilege. In particular, petitioner argued that sealed Exhibit 5-C, which contains tape recordings (known as the MCCS tapes) of two meetings between various attorneys and representatives of L. Ron Hubbard and the Church of Scientology, was protected by the attorney-client privilege. Petitioner also submitted a declaration from Lisa Britowich, one of its representatives, and a declaration from James M.A. Murphy, a tax lawyer who had represented Mr. Hubbard's legal interests in his dealings with petitioner. Pet. 3; Pet. App. 18a; *Zolin*, 109 S. Ct. at 2624.

The IRS argued, among other things, that the MCCS tapes fell within the crime-fraud exception to the attorney-

client privilege.[1] In addition, the IRS submitted to the court sealed declarations by IRS Special Agent Petersell that contained partial transcripts of the MCCS tapes and stated that the excerpts and his discussions with former Church employees had given him reason to believe that the meetings were part of a criminal conspiracy to defraud the United States. Pet. App. 29a-30a; *Zolin*, 109 S. Ct. at 2624.[2]

After oral argument and an evidentiary hearing, the district court ordered production of 5 of the 12 sealed documents. Turning to the MCCS tapes, the district court ruled that petitioner had demonstrated that they contained confidential attorney-client communications, that the privilege had not been waived, and that the crime-fraud

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[1] The attorney-client privilege does not protect communications made in furtherance of a crime or fraud. To invoke that exception, there must be a prima facie showing that the client was engaged in or planning criminal or fraudulent conduct and that the attorney's advice was in furtherance of or closely related to the criminal or fraudulent activity. See, *e.g.*, *Clark* v. *United States*, 289 U.S. 1, 15-16 (1933).

[2] The affidavits alleged that the taped meetings, part of the MCCS (Mission Corporate Category Sortout) project, "focused generally on the intentional violation of the tax laws," specifically, "i) a proposed scheme whereby the Church's cash transfers to Hubbard would be disguised as payments for services rendered (allegedly to insulate Hubbard from tax liability and to protect the Church of Scientology's tax-exempt status), and ii) a proposed scheme whereby Hubbard would be able to control royalty income * * * without that control being traceable to him." Pet App. 29a-30a. In separate litigation, the Tax Court has found that the Church of Scientology engaged in a conspiracy, which lasted from 1969 until at least 1977, to defraud the IRS and obstruct lawful IRS tax administration functions. See *Church of Scientology* v. *Commissioner*, 83 T.C. 381, 429-443 (1984), aff'd, 823 F.2d 1310 (9th Cir. 1987), cert. denied, 486 U.S. 1015 (1988). The Tax Court concluded that "criminal manipulation of the IRS to maintain its tax exemption * * * was a crucial and purposeful element of the [Church's] financial planning." 83 T.C. at 504.

exception to the attorney-client privilege did not apply. Pet. App. 33a-34a. The government sought reconsideration on the ground that the court should not have rejected the applicability of the crime-fraud exception without an in-camera inspection of the complete tapes. The district court denied the motion. Pet. App. 31a-32a.

2. A panel of the court of appeals affirmed the trial court's ruling that the crime-fraud exception was not applicable to the MCCS tapes. Citing *United States* v. *Shewfelt*, 455 F.2d 836, 840 (9th Cir.), cert. denied, 406 U.S. 944 (1972), the panel explained that the crime-fraud exception could be invoked to justify disclosure of otherwise privileged communications only where the government establishes "a prima facie case of fraud *independently* of the said communications." Pet. App. 27a, quoting 455 F.2d at 840. Applying that rule, the panel concluded that the independent evidence in this case—consisting of the special agent's declarations describing his conversations with former Church employees, but not the partial transcripts of the MCCS tapes themselves—was not sufficient to make out the requisite prima facie showing of intended illegality. Pet App. 29a-30a.[3]

The court of appeals ordered the case to be reheard en banc. Following supplemental briefing and oral argument, however, the en banc court entered an order vacating as improvidently granted the previous order granting rehearing en banc and reinstated the panel decision with certain

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[3] On January 24, 1986, during the pendency of the appeal, L. Ron Hubbard died. The court of appeals, however, rejected petitioner's suggestion of mootness because the investigation entails civil elements that have survived Mr. Hubbard's death. See Pet. App. 19a (adopting the reasoning stated in *United States* v. *Author Service, Inc.*, 804 F.2d 1520, 1522 n.1 (9th Cir. 1986)). See also *Zolin*, 109 S. Ct. at 2623 n.3 ("We are satisfied that a live controversy remains.").

modifications. Pet. App. 7a-8a, 16a. Judge Beezer, joined by two other judges, dissented from the en banc court's order. He concluded that rehearing en banc had not been improvidently granted and that the en banc court should overrule the independent evidence requirement of *Shewfelt*. Pet. App. 8a-15a.

This Court granted certiorari to review whether the crime-fraud exception to the attorney-client privilege must be established by the "independent evidence" rule of *Shewfelt* (*i.e.*, without reference to the content of the contested communications themselves), or alternatively, whether the applicability of that exception can be resolved by an in camera inspection of the allegedly privileged material. *Zolin*, 109 S. Ct. at 2623.[4] In a unanimous opinion, this Court rejected the Ninth Circuit's "independent evidence" approach and held that in camera review may be used to determine whether allegedly privileged attorney-client communications fall within the crime-fraud exception. *Ibid.* In so ruling, this Court held that before a district court may engage in in-camera review at the request of the party opposing the privilege, that party "must present evidence sufficient to support a reasonable belief that *in camera* review may yield evidence that establishes the exception's applicability." *Id.* at 2632. Finally, this Court held that "the threshold showing to obtain *in camera* review may be met by using

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[4] This Court also granted certiorari on a wholly separate issue, *viz*, whether a district court may place restrictions on the IRS regarding the disclosure of summoned information. *Zolin*, 109 S. Ct. at 2622-2623. The district court's enforcement order had provided that the documents produced pursuant to the summons "shall not be delivered to any other government agency by the IRS unless criminal tax prosecution is sought or an Order of Court is obtained." Pet App. 35a. The court of appeals upheld that restriction (Pet. App. 24a-25a) and this Court affirmed its judgment on that issue by an equally divided Court (*Zolin*, 109 S. Ct. at 2622-2623). The disclosure issue is not now before the Court.

any relevant evidence, lawfully obtained, that has not been adjudicated to be privileged." *Ibid.*[5] Because the court of appeals had employed a "rigid independent-evidence requirement which categorically excluded the partial transcripts and the tapes themselves from consideration," this Court vacated that judgment and remanded for further proceedings consistent with its opinion. *Ibid.*

3. On remand, the court of appeals directed the parties to file supplemental briefs on the crime-fraud issue. In accordance with this Court's remand instructions in *Zolin*, 109 S. Ct. at 2632 n.13, the court of appeals examined the partial transcripts, along with the independent evidence already reviewed in its first opinion, and concluded that there was "sufficient evidence of intended illegality to establish that the tapes are within the crime-fraud exception." Pet. App. 3a-4a. In so ruling, the court of appeals stated that the "partial transcripts demonstrate that the purpose of the MCCS project was to cover up past criminal wrong-doing, * * * [that the] MCCS project involved the discussion and planning of future frauds against the IRS in violation of 18 U.S.C. § 371, * * * [and that the] figures involved in MCCS admit on the tapes that they are attempting to confuse and defraud the U.S. Government." Pet. App. 4a. The court of appeals accordingly concluded that "[o]n remand the district court should admit the MCCS tapes into evidence,

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[5] IRS Special Agent Petersell stated that the partial transcripts of the MCCS tapes were obtained by the IRS from a confidential source prior to the issuance of the summons and that that source was not a party to the *Armstrong* litigation in the California Superior Court. See *Zolin*, 109 S. Ct. at 2624 n.5. In view of the district court's failure to make any finding to the contrary, this Court assumed for purposes of its decision that the transcripts were legally obtained. *Ibid.*

subject to any objections the parties might make at that time." *Ibid.*[6]

ARGUMENT

Petitioner contends that the court of appeals erred in ruling, after remand from this Court in *United States* v. *Zolin*, 109 S. Ct. 2619 (1989), that the MCCS tapes fall within the scope of the crime-fraud exception to the attorney-client privilege. The court of appeals' decision, however, reflects a correct application of the principles of law discussed in this Court's opinion in *Zolin* to the particular facts of this case. Indeed, the court of appeals concluded on remand (Pet. App. 4a) that the individuals involved in the MCCS project "admit on the tapes that they are attempting to confuse and defraud the U.S. Government." It is therefore apparent that the MCCS tapes are well within the scope of the crime-fraud exception. Moreover, the issue here is presented in the context of a

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[6] Petitioner did not seek a stay of the court of appeals' mandate pending the filing of a petition for a writ of certiorari. Following the issuance of the mandate, the district court held a hearing and ordered the MCCS tapes to be released to the government. Copies of the tapes were then turned over to the IRS. Petitioner, however, has filed a motion for reconsideration of the trial court's enforcement order. The district court has scheduled a hearing on this matter for February 25, 1991; it has also "stayed" its enforcement order pending that hearing. Because this is an IRS summons enforcement proceeding, the government has sought only to obtain access to the MCCS tapes for purposes of its tax investigation, and not to admit them into evidence. Thus, as the district court properly observed on remand, "there is no point in receiving the tapes 'into evidence' since the Court of Appeals has made the only relevant finding of fact—that is, that the tapes demonstrate that the tapes come under the crime-fraud exception to the attorney-client privilege rule, and should, therefore, be subject to the IRS summons." Order of Jan. 17, 1991, at 1-2.

unique factual situation (the MCCS project) that is not likely to be repeated. Nor does the court of appeals' decision conflict with any decision of this Court or of another court of appeals. Accordingly, further review is not warranted.

1. Petitioner argues (Pet. 7, 9-10) that the court of appeals applied an incorrect standard of review in determining that the crime-fraud exception applies in this case. Thus, petitioner maintains that the court of appeals improperly reviewed the district court's crime-fraud findings under a de novo standard, rather than under the more restrictive "abuse of discretion" or "clear error" standards. Petitioner also urges that "this Court should explicitly reject the *de novo* standard of review applied below." *Id.* at 15.

Petitioner's arguments are refuted by the express language of this Court's opinion in *Zolin*. Contrary to petitioner's contentions, this Court's opinion in *Zolin* contemplated that the court of appeals would determine certain issues on remand. In particular, this Court's opinion states that the court of appeals should consider whether the partial transcripts themselves were sufficient to establish the crime-fraud exception. As the Court explained (109 S. Ct. at 2632 n.13):

> The Court of Appeals also will have the opportunity to review the partial transcripts, and to determine whether, even without *in camera* review of the [actual] tapes, the IRS presented sufficient evidence to establish that the tapes are within the crime-fraud exception.

Contrary to petitioner's assertions, this is exactly what the court of appeals did on remand in "examin[ing] the transcripts and [in] determin[ing] * * * [that] they, along with the independent evidence already reviewed, demonstrate sufficient evidence of intended illegality to

establish that the tapes are within the crime-fraud exception." Pet. App. 3a-4a.[7]

Petitioner's further argument (Pet. 10-12) as to the proper standard of appellate review to be applied to district court determinations in crime-fraud cases is beside the point. This case does not present such an issue. Rather, as discussed, this Court's opinion in *Zolin* contemplated that the court of appeals on remand would make certain determinations in the first instance. The court of appeals' decision below is fully in accord with this Court's opinion. In these circumstances, this case is not a proper vehicle to resolve the standard of review questions raised by petitioner. Indeed, the decision below has little, if anything, to do with such matters.[8]

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[7] In a similar vein, petitioner's reliance (Pet. 20 n.12) on the crime-fraud ruling in *Church of Scientology* v. *Armstrong*, No. C420 153 (Cal. Super. County Ct. Feb. 11, 1985), is misplaced. That case was decided under California law and not under the federal crime-fraud standards set forth in this Court's decision in *Zolin*.

[8] At all events, even under a deferential standard of review, the district court plainly erred in concluding that the evidence failed to establish the crime-fraud exception. Here, the trial judge stated at the April 30, 1985, hearing that he failed to see how retroactively reversing a transaction for tax purposes "necessarily show[ed] a fraud or a crime." Tr. 79. An individual violates 18 U.S.C. 371, however, by conspiring to defraud the United States through disruption of the IRS's lawful functions in assessing and collecting federal income taxes. Thus, contrary to the district court's conclusion below, a conspiracy against the IRS plainly can encompass a transaction where the conspirators retroactively generate false documents to mislead the IRS about the true nature of a transaction. See *United States* v. *Carruth*, 699 F.2d 1017, 1021 (9th Cir. 1983), cert. denied, 464 U.S. 1038 (1984) (tax shelter promoters convicted under 18 U.S.C. 371 for selling tax shelters based on nonexistent cattle breeding transactions). See also Pet. App. 4a.

2. Petitioner next argues (Pet. 18) that the court of appeals erred in determining that the crime-fraud exception to the attorney-client privilege applied here because it allegedly reached its decision without reviewing the evidence submitted by petitioner in the trial court. The record as a whole, however, fails to support that argument. Although this Court's opinion stated that the partial transcripts alone might be sufficient to establish the crime-fraud exception (109 S. Ct. at 2632 n.13), there is no basis for thinking that the court of appeals on remand did not consider petitioner's evidence for whatever value it might have.

Contrary to petitioner's assertion, the court of appeals directed the parties on remand to file supplemental briefs on several questions, including the question it decided here, *i.e.*, whether, without in-camera review of the tapes themselves, the government presented sufficient evidence to establish whether the tapes were within the scope of the crime-fraud exception. Petitioner's brief on remand (at 10-16) contains an extensive discussion of the evidence submitted by the government and the rebuttal evidence submitted by petitioner on the crime-fraud issue. Petitioner does not deny that the court of appeals had this brief before it in rendering its decision on remand. Hence, the fact that the court of appeals did not expressly discuss petitioner's evidence in its opinion falls far short of demonstrating that the court did not consider petitioner's arguments. Indeed, the declarations relied on by petitioner here (Pet. 22-23) are general in nature and make no attempt whatsoever to explain the specific discussions of crimes contained on the partial transcripts.[9] In these circumstances, it is apparent that

[9] For example, the Declaration of MCCS staff member Lisa Britowich merely alleges in general terms that the MCCS meetings "were definitely considered attorney-client conferences which were fully intended to be confidential and privileged." Supp. E.R. at 3. Similarly,

the result here would not have been any different had the court of appeals chosen to discuss petitioner's evidence in its opinion on remand.[10]

3. Finally, petitioner urges (Pet. 8, 21-28) that the conversations reflected on the MCCS tapes represent nothing more than candid and frank discussions between attorneys and their clients on how to restructure past business and corporate relationships to avoid problems in the future. From this premise, petitioner urges (Pet. 7-8) that review by this Court is necessary so that attorneys and clients will be free to discuss such matters without the fear that their communications will be divulged to their adversaries. The argument is misconceived.

The attorney-client privilege was not designed to protect communications made in furtherance of a fraud or crime. It is the purpose of the crime-fraud exception to assure that the seal of secrecy does not extend to communications " 'made for the purpose of getting advice for the commission of a fraud' or crime." *Zolin*, 109 S. Ct. at 2626, quoting *O'Rourke* v. *Darbishire*, [1920] A.C. 581, 604. In the

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the Declaration of James M.A. Murphy, an attorney for Mr. Hubbard, asserts generally that he gave legal advice on "whether certain things had been handled properly in the past and how they should be handled in the future" and that there was "never any question * * * [whether] we were being consulted for criminal or fraudulent purposes." *Id.* at 8. However, neither of these declarations speaks specifically to the IRS special agent's allegations that the MCCS project focused on the intentional violation of the tax laws, specifically on a proposed scheme whereby the Church's cash transfers to Hubbard would be disguised as payments for services rendered and a proposed scheme whereby Hubbard would be able to control royalty income without that control being traceable to him. See Pet. App. 29a-30a and note 2, *supra*.

[10] Any remaining possibility that the panel might have overlooked petitioner's evidentiary arguments is eliminated by the fact that petitioner repeated those arguments in its petition for rehearing with suggestion for rehearing en banc.

present case, the court of appeals carefully reviewed the communications reflected on the partial transcripts and concluded (Pet. App. 4a) that the "purpose of the MCCS project was to cover up past criminal wrong-doing" and that the "MCCS project involved the discussion and planning of future frauds against the IRS, in violation of 18 U.S.C. § 371." See *United States* v. *Carruth*, 699 F.2d 1017, 1021 (9th Cir. 1983), cert. denied, 464 U.S. 1038 (1984). That conclusion is clearly correct and no further review is warranted.[11]

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[11] Petitioner makes a number of factual arguments (Pet. 23-26) in support of its contention that the MCCS tapes show no planning or furtherance of a future crime or fraud. We note, however, that the partial transcripts from which petitioner quotes were filed under a sealing order in the district court. We do not think it appropriate to discuss such confidential matters here. If, however, the Court wishes the government to respond to petitioner's assertions, we will do so under seal. At all events, the excerpts quoted by petitioner distort the actual statements made by the parties on the sealed transcripts. Indeed, as mentioned, the court of appeals found that the individuals involved in the MCCS project "admit on the tapes that they are attempting to confuse and defraud the U.S. Government." Pet. App. 4a. Petitioner's self-serving speculation and conjecture on this matter do not raise any issue for this Court to review.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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